VAKIFBANK TURKISH ECONOMY WEEKLY

Turkish budget has continued its positive performance in the first quarter of 2011

VakıfBank

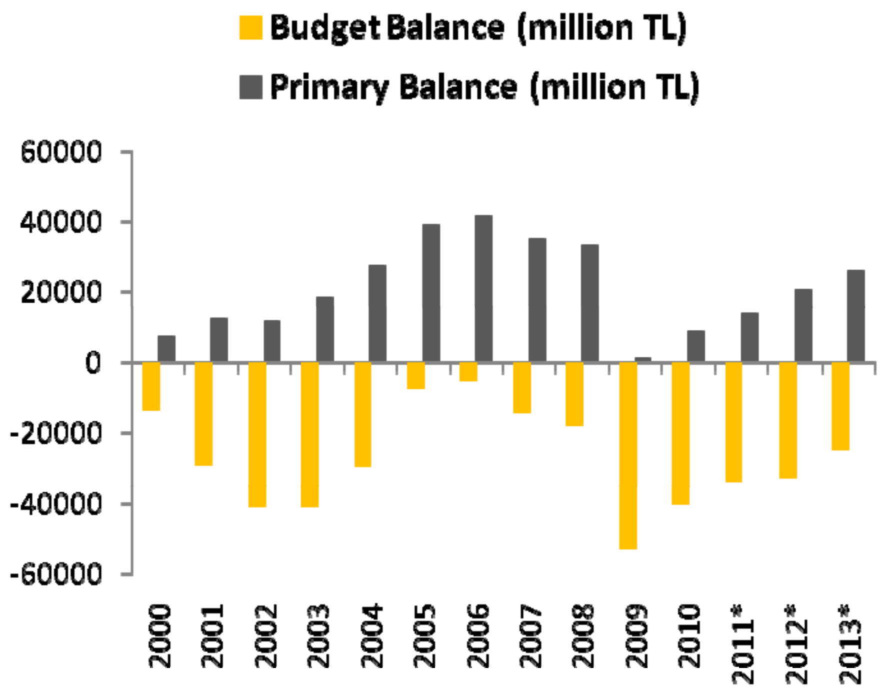
T. Vakıflar Bankası T.A.O

25 April 2011

No: 25

Vakıfbank Economic Research

Turkey posted a budget deficit below Medium Fiscal Plan target…



Source: Republic of Turkey Ministry of Finance
*2011,2012,2013: Medium-Term Fiscal Plan Expectations

In the Medium Term Fiscal Plan for 2011-2013, budget deficit to GDP ratio is expected to decrease to 2.8% in 2011, to 2.4% in 2012 and 1.6% in 2013.

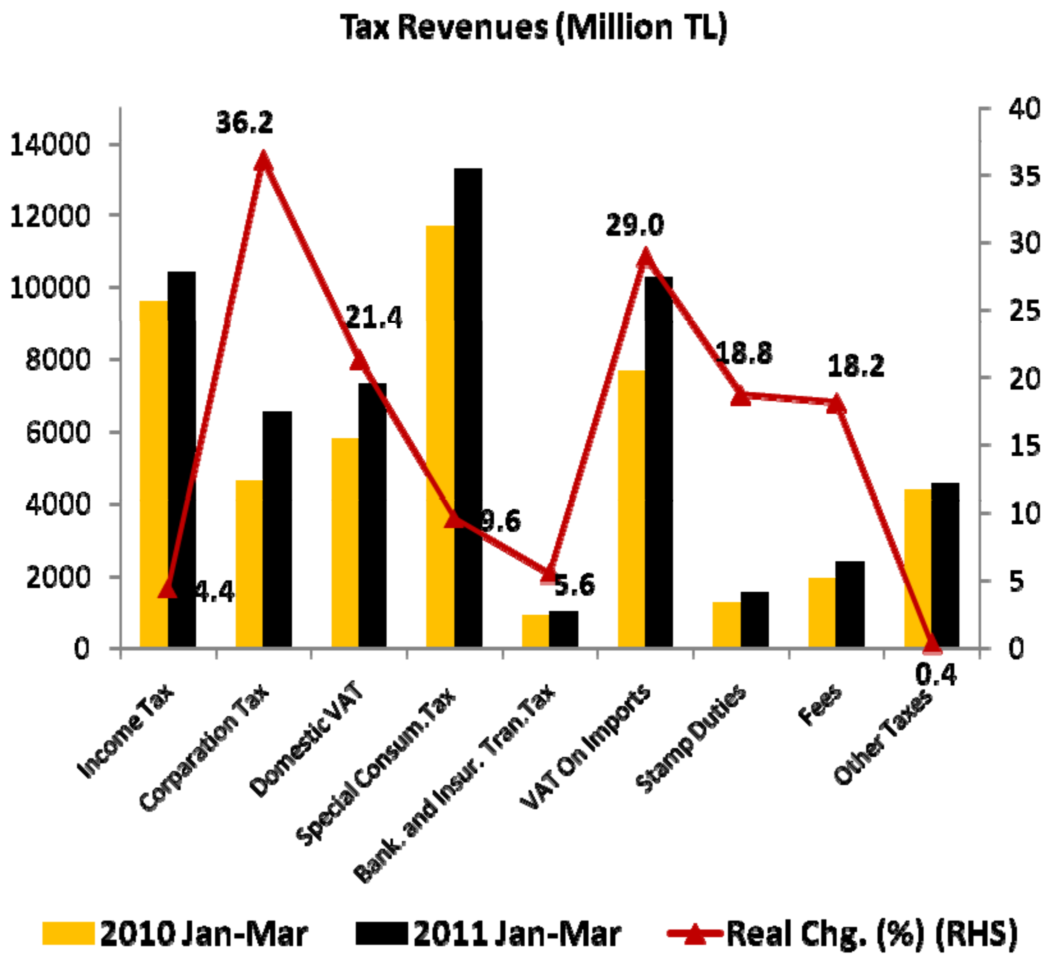
- Although global economy has continued to recover since the beginning of 2011, sovereign risks have increased significantly throughout the world. Major risks towards the global economy could be classified as;
  - Eurozone's debt crisis,
  - US's high public debt and slow recovery in housing and employment markets,
  - High commodity prices.
- Despite the concerns on sustainability of high public debt levels and budget deficits of advanced economies, Turkey sustains its positive performance in terms of deficit and government debt-to-GDP ratios. Turkey posted a budget deficit equivalent to 3.6 % of GDP in 2010, below a target of 4% of GDP in Medium Fiscal Plan.

Smaller budget deficit is driven by the limited expenditure and strong revenue growth...

- Budget deficit in Q1 2011 was realized as TL 4.124 billion. For Q1, the budget deficit decreased by 65% in real term compared to Q1 2010.
- Primary surplus increased by approximately 3 times and reached to TL 9.844 billion in the same period.
- In Q1 2011, budget expenditures increased by 2.5% and the budget revenues increased by 15.9% in real terms compared to the same period of the previous year. Therefore the fast growth rate in revenues was notable for the strong fiscal stance.

January – March						
(Billion TL)	2010	2011	Chg. (%)	Real Chg. (%)*	2011 Realization Target	Ratio of Realization (%)
Expenditures	68.373	72.853	6.55	2.46	312.573	23.31
1) Excluding Interest	53.374	58.885	10.33	6.10	265.073	22.21
Compensation of Employees	16.224	18.774	15.72	11.28	72.299	25.97
Govern. Prem. to Soc. Sec. Agen.	2.754	3.309	20.15	15.54	12.737	25.98
Good and Services Procurements	4.202	4.774	13.61	9.25	30.049	15.89
Current Transfers	27.719	29.554	6.62	2.53	115.778	25.53
Capital Expenditures	1.012	1.499	48.12	42.44	21.698	6.91
Capital Transfers	0.281	0.265	-5.69	-9.31	4.3	6.16
Lending	1.181	0.709	-39.97	-42.27	6.436	11.02
2) Interest	48.296	14.999	-68.94	-70.13	47.5	31.58
Revenues	57.032	68.729	20.51	15.89	279.026	24.63
Tax revenues	47.902	57.45	19.93	15.33	232.22	24.74
Other revenues	9.13	11.279	23.54	18.80	46.806	24.1
Budget Deficit	11.341	4.124	-63.64	-65.04	33.546	12.29
Primary Surplus	3.659	9.844	169.04	158.72	13.954	70.55
Source: Minister of Finance						
*: Real changes depend on Fisher equation						

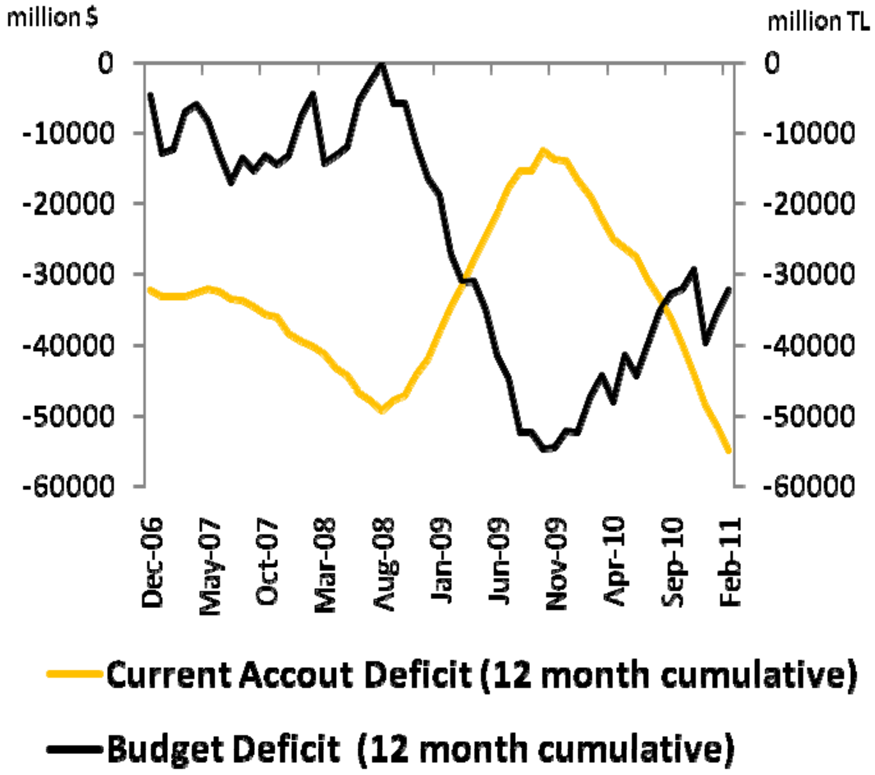
Higher domestic demand boosted the tax revenues in Q1 2011...



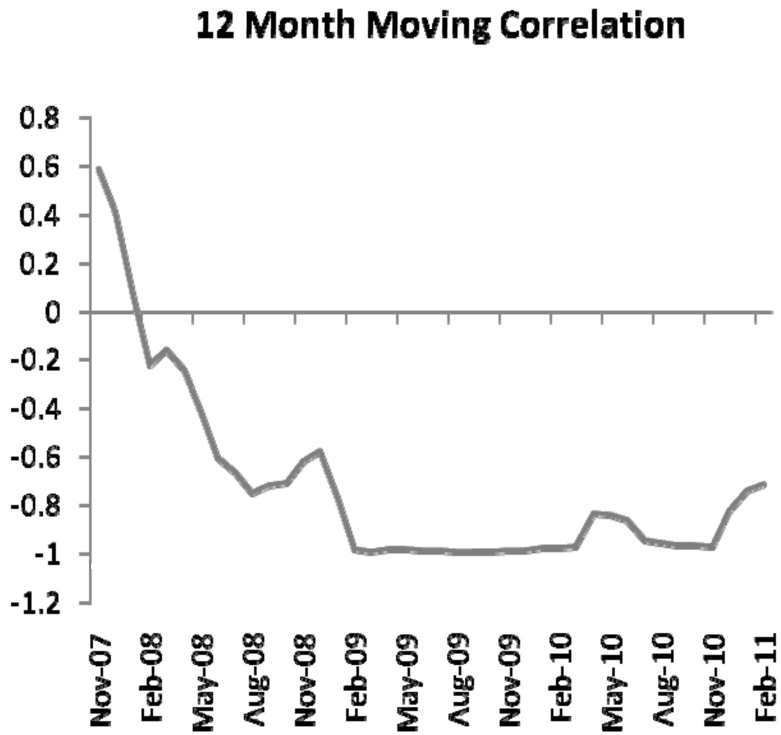
Source: Minister of Finance

- In the budget realizations of Q1, the most remarkable development has been the increase in tax revenues.
- Due to strong economic recovery in Q1 2011, tax revenues increased by 15.3% in real terms.
- With the strong domestic demand, VAT on import increased by 29% in real terms and Domestic VAT income exhibited strong performance with 21.4% increase.
- Since the strong growth in industry continues in the first two months of 2011, increase in tax collection does not appear to be a surprise.

The relationship between budget deficit and current account deficit...



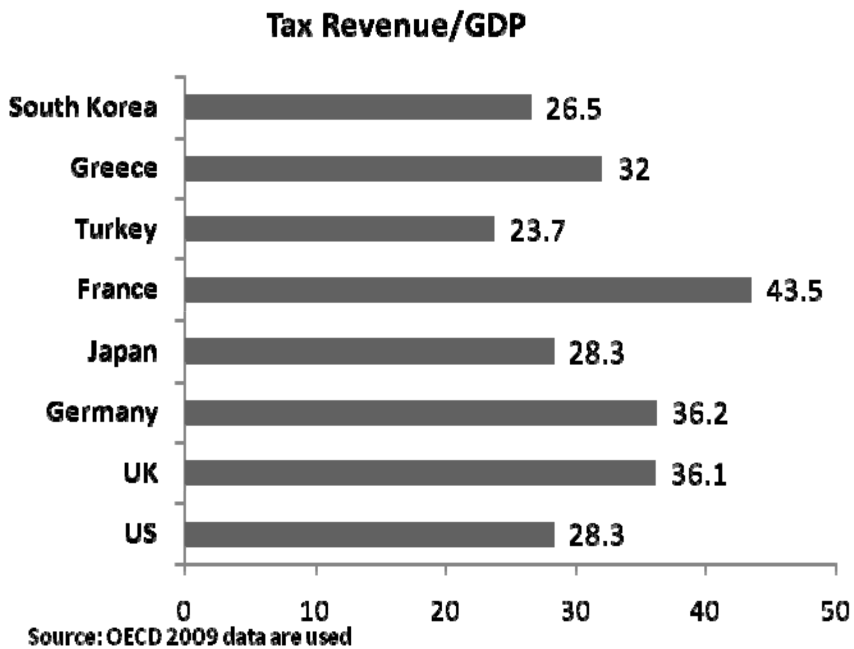
Source:CBRT

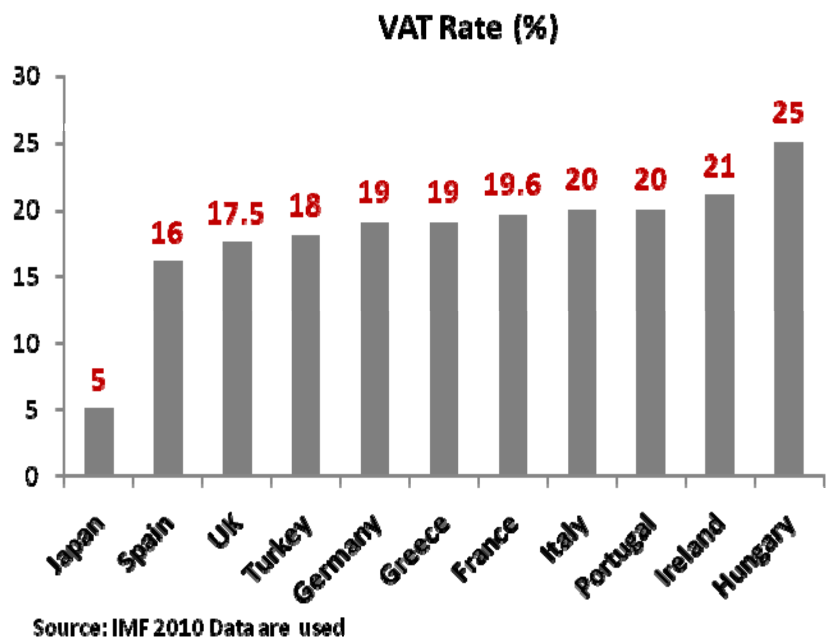


Source:CBRT

During the recent crisis due to the contraction in trade deficit, current account deficit (CAD) declined and expansionary fiscal policies was followed by the increase in budget deficit. This leads to a negative relationship between CAD and budget deficit. Moreover, recent recovery in domestic demand after the crisis leads to widen CAD by the time increasing tax collection also improves the budget performance. Especially, increasing CAD makes VAT on imports rise and this also improves the negative relationship between budget deficit and CAD.

Although tax revenue has continued to rise in Turkey, the tax revenue/GDP ratio is lower than many countries...

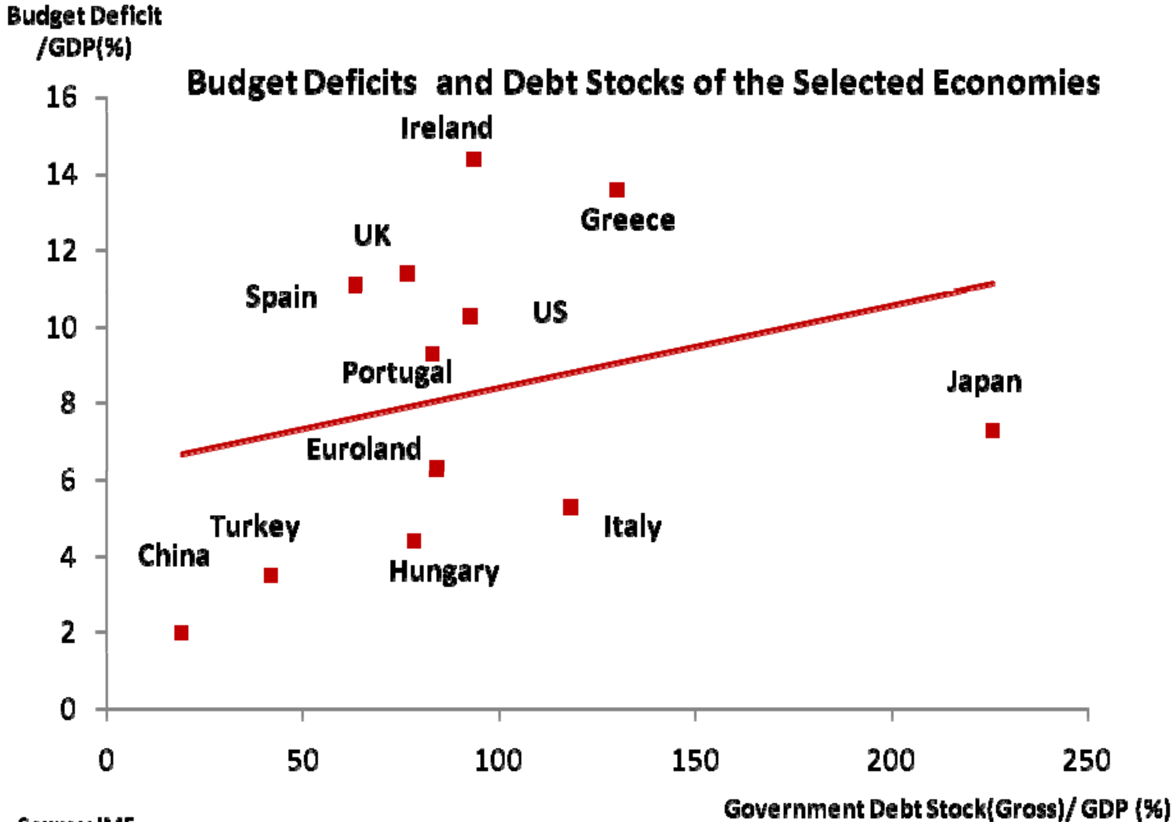




- The low levels of Turkey’s tax revenue/GDP ratio compared to other countries could be explained by high levels of informal economy. Besides the RHS graph shows that Turkey’s VAT rate level is almost the same with many other countries.

- One of the Turkey’s major structural problems is the high levels of informal economy. Other problems could be defined as, not having broad-based and equatible tax system, major part of tax revenue being acquired through indirect taxes, and lower direct tax levels than the world standards.

Sovereign risks due to high public deficits still continue to be a problem in 2011...



Source: IMF

- With the effect of the fiscal measures taken in 2010, budget deficit to GDP ratios continue to rise in many developed countries. In addition to the concerns on sustainability of high public debt levels and public deficits of Euro Zone, the government debt stock to GDP ratio reached to record high level of 92.7% in US and 225.9% in Japan.

- On the other hand, the budget deficit and government debt stock in emerging countries like Turkey recovered quickly after crisis. Turkey with its fast economic growth has the lowest budget deficit and debt stock ratio after China.

Serkan Özcan
Chief Economist
+ 90 312 455 7087
serkan.ozcan@vakifbank.com.tr

Cem Eroğlu
Senior Economist
+ 90 312 455 8480
cem.eroglu@vakifbank.com.tr

Seda Meyveci
Economist
+ 90 312 455 8485
seda.meyveci@vakifbank.com.tr

Halide Pelin Kaptan
Researcher
+ 90 312 455 8483
halidepelin.kaptan@vakifbank.com.tr

Emine Özgü Özen
Researcher
+ 90 312 455 8487
Emineozgu.ozen@vakifbank.com.tr

Senem Güder
Reseacher
+ 90 312 455 8476
senem.guder@vakifbank.com.tr

T. Vakiflar Bankasi T.A.O
Ataturk Bulvari No: 207
Kavaklidere 06683 Ankara, Turkey
www.vakifbank.com.tr

Vakifbank Economic Research
ekonomik.arastirmalar@vakifbank.com.tr